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To: Each Supervisor

From: Dave Lambertson
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Subject: **ENERGY UPDATE REPORT**

This is the twelfth in a series of regular reports requested by your Board to provide updates on the County's ongoing energy management activities. These reports are provided quarterly and discuss the status of key energy related issues and responses to Board Motions and requests.

Electricity Rates

SCE rates during this year will be impacted by two factors: the removal of the rate surcharge and SCE's general rate case. These are each explained below.

Southern California Edison (SCE) Surcharge Removal

On July 10, 2003, the California Public Utilities Commission (CPUC) approved SCE's request to remove a portion of the 4-cent per kilowatt-hour (kWh) surcharge imposed on retail customers in early 2001. SCE was allowed to add the surcharges in early 2001 to help pay off debt they incurred procuring energy for their customers during the energy crisis of 2000-01. The new rates took effect on August 1, 2003.

The overall impact for all customers is approximately \$1.25 billion annually. The percent of savings varies by type of accounts and class. The average savings for each class is as follows:

- Residential, 7.8% rate reduction
- Small Commercial, 12.8% rate reduction
- Medium Commercial, 16.9% rate reduction
- Industrial, 18.9% rate reduction
- Agricultural, 15% rate reduction
- Street Lighting, 15.6% rate reduction
- SCE System-wide, 12.9% rate reduction

The new rates will be in effect for a minimum of 1 year, at which time new rates are anticipated to be established through SCE's General Rate Case.

Assuming the prior year consumption pattern, the savings in the ISD Utilities Budget is approximately \$6.0 million in fiscal year 2003/04.

SCE General Rate Case

Under their General Rate Case, SCE has requested new rates at the CPUC. In Phase 1 of the Rate Case, SCE asked the CPUC to increase their revenues by about \$248 million per year to cover increased operating and maintenance expenses on their system and higher overhead costs. The Commission has yet to render an opinion on that issue.

Phase 2 of the Rate Case is now proceeding and will determine how SCE's revenue requirement for its operating and maintenance, distribution, and generation costs (approximately \$6 billion) will be allocated. SCE's initial proposal, if adopted, on an average, would impact the customer classes as follows:

- Residential, 17.8% rate increase
- Small Commercial, 8.18% rate increase
- Medium Commercial, 7.14% rate reduction
- Industrial, 9.27% rate reduction
- Agricultural, 24.12% rate increase
- Street lighting, 15.6% rate increase

Residential, small commercial, street lighting, and agricultural pumping customers would see rate increases. Medium commercial and industrial customers would see rate decreases. The net impact to the ISD managed utility costs is currently being analyzed. However, early estimates indicate that we should experience savings of between \$2 to \$3 million per year. Phase 2 includes testimony and cross-examination by intervening parties. The County, through ISD, has intervened in the Rate Case. The County, along with other large retail customers (including the Los Angeles Unified School District) have jointly filed testimony at the CPUC that, if adopted by the CPUC, would result in even greater rate decreases for the County. The Utility Reform Network (TURN) and the CPUC's Office of Ratepayer Advocates (ORA) have provided testimony seeking to minimize rate increases for residential customers.

We will keep your Board apprised of significant events or issues taking place in this proceeding. Any new rates that the CPUC approves will not go into effect earlier than August 1, 2004.

\$1 Billion Refund from Department of Water Resource Purchases

On September 4, 2003, the CPUC approved a refund to all ratepayers of the State's investor owned utilities by approving a \$1 billion reduction to the revenue requirement of the California Department of Water Resources (DWR). The reason for the refund is that DWR issued \$1 billion in additional bonds last year to provide reserves in case the state had to continue buying power for the utilities beyond 2002. The transition from DWR buying power to the utilities buying power was successfully concluded at the end of 2002. Once it was determined that this surplus was available, the CPUC, DWR, and the Governor's office structured the refund.

The CPUC has ordered that the \$1 billion refund should be returned to ratepayers on a one-time basis. The refund will be disbursed across all rate classes and customers equally at \$0.006/kWh based on total kWh consumption for the time period from August 1, 2002 through July 31, 2003. The funds will be returned as a credit on customers' bills and is required to be completed within 45 days from September 4, 2003.

SCE customers' share of the refund is \$422 million. The impact on ISD Utilities Budget for FY 2003-04 will be a one-time credit of approximately \$2 million.

Federal Energy Regulatory Commission (FERC) Investigation into Price Manipulation in Western Markets

Complaint Against El Paso Corporation

As authorized by your Board, in July 2003, the County entered into a settlement agreement with El Paso Corporation and its affiliates (El Paso) to resolve all lawsuits against El Paso at FERC and State court related to El Paso's alleged wrongful conduct in the sale and delivery of natural gas and electricity. Other parties to these lawsuits, including the Attorney General of the State of California, the CPUC, and the City of Los Angeles, have also settled with El Paso and entered into a global settlement agreement. The global settlement agreement is subject to approval by the courts and regulatory authorities, including FERC.

El Paso's obligations to make payments to the County under the County's settlement will occur only after these approvals take place. The hearing on the approval of the global settlement is currently scheduled for November 20, 2003 in San Diego Superior Court. FERC has not yet approved the global settlement; however, it is expected to hear the matter soon. We anticipate that the earliest the County will receive its initial payment under the settlement is in the first quarter of 2004.

California Demand for Refunds

California's demand for \$9 billion in refunds is very unlikely to be met. At the current time, FERC has authorized refunds that ultimately could reach \$1 billion. The California parties have requested that FERC reconsider this amount, but most believe it is unlikely that the amount will change significantly absent a court ruling requiring additional refund amounts.

Renegotiation of Long Term Contracts

By a 2-1 vote, FERC has concluded that it will not allow California and other parties to obtain lower prices in the long-term contracts entered into at the height of California's energy crisis. FERC concluded that the "sanctity" of contracts was more important than reforming these long-term arrangements. FERC has been asked to reconsider its decision; but it is unlikely that FERC will do so and this issue ultimately may be decided by the courts.

Market Manipulation Investigation

This proceeding is ongoing. FERC is still exploring the extent to which Enron, in partnership with a number of other parties, including California municipal utilities, "gamed" the market. One possible remedy from this proceeding (as well as other proceedings investigating whether there was a "physical withholding" of power from the market) is "disgorgement" of profits made as a function of these activities. The amounts that could be refunded are too speculative at this time to address.

SCE/CPUC Settlement Agreement

The California Supreme Court issued its decision on August 21, 2003 regarding the settlement of the federal lawsuit between SCE and the CPUC involving electricity rates that SCE charges its ratepayers. The settlement agreement entered into in early 2001 established the \$0.04/kWh surcharge on all customers to offset procurement losses incurred by the utilities. The Utility Reform Network (TURN) filed an appeal to the Ninth Circuit Court of Appeals challenging the district court's decision to uphold the settlement. The Ninth Circuit declined to make a definitive decision and referred the question of the legality of the settlement to the California Supreme Court because the Ninth Circuit believed it was a state law issue.

The California Supreme Court has now ruled that the settlement did not violate State law. The ruling by the California Supreme Court sets the stage for the Ninth Circuit to act expeditiously in issuing a decision upholding the settlement in a manner consistent with the California Supreme Court's guidance.

Natural Gas

As previously reported to your Board starting August 1, 2003, ISD entered into three-fixed price, variable term contracts with the California Department of General Services' natural gas purchasing pool for a portion of natural gas supplied under the ISD Utility Budget. The table below describes conditions of the contract:

Volume Amount	Price (\$/MMBtu)	Term
One-third	\$5.42	8/03 thru 6/04
One-third	\$5.28	8/03 thru 6/05
One-third	\$5.18	8/03 thru 6/06

(MMBtu = million British Thermal Units)

This strategy protects the County from recent natural gas market price volatility and provides budget stability for fiscal year 2002-03 and a measure of stability for the following two fiscal years. Under this pricing arrangement, the overall price for natural gas for fiscal year 2003-04 is fixed at \$5.30/MMBtu; slightly below the original budget assumption of \$5.50/MMBtu.

These gas purchases are for the County's large facilities (e.g., power plants, hospitals, jails). The Pitchess cogeneration plant continues to be supplied on an index-based contract and reimbursed by SCE at cost.

Retrofit Projects

ISD has essentially completed the retrofit projects approved by your Board on May 28, 2002 totaling \$4.1 million. These projects included lighting and lighting controls installations at the Music Center, Olive View Hospital, Museum of Natural History, Central Juvenile Hall and Courthouses in Compton, San Fernando, Beverly Hills, Long Beach, Norwalk, and Malibu. The only project remaining is at the Registrar-Recorder headquarters. At the customer's request, that project has been put off until after the general election in March 2004.

ISD has nearly completed retrofit projects funded by the CPUC's \$3.3 million grant under their 3rd Party Local Energy Efficiency Program for 2002 and 2003. The projects include lighting and lighting control retrofits, variable speed drive installations on building fan motors, and a new chiller at Harbor/UCLA Hospital. This work is expected to be completed by the end of calendar year 2003.

ISD is applying for further funding from the CPUC's 3rd Party Local Energy Efficiency Program for calendar years 2004 and 2005. ISD will be partnering with SCE and The Gas Company on a 3rd Party/Utility joint proposal. The CPUC's program instructions had recommended such partnering arrangements. ISD's proposal seeks to continue

implementing cost effective retrofit programs. Additionally, ISD is requesting funding to begin a building retro commissioning (RCx) program. RCx programs aim to make relatively minor operating, maintenance, and upgrade improvements to existing building systems – primarily heating and air conditioning systems. Typical RCx programs conducted by other entities indicate average RCx facility costs of anywhere from \$0.10 to \$1.00 per square foot of building space with energy savings generated paybacks of 1 to 5 years.

Community Choice Aggregation (CCA) – AB 117

CPUC Order Instituting Rulemaking

On September 10, 2003, the CPUC ordered a rulemaking proceeding to establish the rules and regulations for CCA. CCA was created as a result of last year's Assembly Bill 117 which permits local governments, cities, and counties to purchase and sell electricity on behalf of utility customers in their jurisdictions after they have registered with the CPUC.

The order was fairly specific about certain rules associated with establishing and operating a CCA. While the CCAs will be involved with purchasing electricity, the investor-owned electric utilities will still provide transmission and distribution services, billing, metering, and the primary aspects of customer service. In order to become a CCA, a city or county must meet certain obligations, including filing an implementation plan and statement of intent, meeting the renewable portfolio standard obligation, fulfilling insurance and bond requirements, and ensuring consumer protection and notification. CCA is an "opt out" program; i.e., customers within a local government's jurisdiction will be considered part of the program unless they actively request not to participate ("opt out").

The County has applied to be a member of a pilot study to be conducted by Navigant Consulting, Inc. (Navigant) and funded by a grant from the California Local Government Commission. The grant program provides for a degree of "matching funds" to study the feasibility of CCA and, if feasible, establish a program proposal. At this point, ISD would contract with Navigant only to conduct a technical study to assess the economic feasibility of purchasing power from a third party for ISD's utility customers and other customers. The grant program also provides that Navigant will participate in the proceeding by monitoring and reporting on activities at the proceeding and filing comments that are mutually beneficial to all pilot study members. The County also intends to intervene in this proceeding in order to provide any comments that are exclusively beneficial to the County.

If you have any questions on any of these issues, please contact me or have your staff contact Howard Choy at (323) 881-3939.

DL:HWC:ynj

c: Chief Administrative Officer
Each Department Head
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